

2003 DRAFTING REQUEST

Bill

Received: **03/10/2003**

Received By: **btradewe**

Wanted: **As time permits**

Identical to LRB:

For: **Alvin Ott (608) 266-5831**

By/Representing: **Beata Kalies**

This file may be shown to any legislator: **NO**

Drafter: **btradewe**

May Contact:

Addl. Drafters:

Subject: **Agriculture - miscellaneous**

Extra Copies:

Submit via email: **YES**

Requester's email: **Rep.Ott@legis.state.wi.us**

Carbon copy (CC:) to:

Pre Topic:

No specific pre topic given

Topic:

Modify the agricultural producer security program

Instructions:

See Attached

Drafting History:

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/?							State
/1	btradewe 04/10/2003	csicilia 04/16/2003 csicilia 04/23/2003	rschluet 04/23/2003		amentkow 04/23/2003		State

04/30/2003 07:48:35 AM

Page 2

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/2	btradewe 04/29/2003	csicilia 04/29/2003	pgreensl 04/29/2003	_____	amentkow 04/29/2003	sbasford 04/30/2003 sbasford 04/30/2003	State

FE Sent For:

<END>

At
intro.

2003 DRAFTING REQUEST**Bill**Received: **03/10/2003**Received By: **btradewe**Wanted: **As time permits**

Identical to LRB:

For: **Alvin Ott (608) 266-5831**By/Representing: **Beata Kalies**This file may be shown to any legislator: **NO**Drafter: **btradewe**

May Contact:

Addl. Drafters:

Subject: **Agriculture - miscellaneous**

Extra Copies:

Submit via email: **YES**Requester's email: **Rep.Ott@legis.state.wi.us**

Carbon copy (CC:) to:

Pre Topic:

No specific pre topic given

Topic:

Modify the agricultural producer security program

Instructions:

See Attached

Drafting History:

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/?							State
/1	btradewe 04/10/2003	csicilia 04/16/2003	rschluet 04/23/2003		amentkow 04/23/2003		State
		csicilia 04/23/2003					

04/29/2003 03:53:58 PM

Page 2

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/2	btradewe 04/29/2003	csicilia 04/29/2003	pgreensl 04/29/2003	_____	amentkow 04/29/2003		State

FE Sent For:

<END>

2003 DRAFTING REQUEST**Bill**Received: **03/10/2003**Received By: **btradewe**Wanted: **As time permits**

Identical to LRB:

For: **Alvin Ott (608) 266-5831**By/Representing: **Beata Kalies**This file may be shown to any legislator: **NO**Drafter: **btradewe**

May Contact:

Addl. Drafters:

Subject: **Agriculture - miscellaneous**

Extra Copies:

Submit via email: **YES**Requester's email: **Rep.Ott@legis.state.wi.us**

Carbon copy (CC:) to:

Pre Topic:

No specific pre topic given

Topic:

Modify the agricultural producer security program

Instructions:

See Attached

Drafting History:

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/?							State
/1	btradewe 04/10/2003	csicilia 04/16/2003 csicilia 04/23/2003	rschluet 04/23/2003		amentkow 04/23/2003		State

4/29 12:45 4/29 03
 4/29 12:45 4/29 03
 4/29 12:45 4/29 03
 4/29 12:45 4/29 03

04/23/2003 12:42:00 PM

Page 2

FE Sent For:

<END>

2003 DRAFTING REQUEST**Bill**Received: **03/10/2003**Received By: **btradewe**Wanted: **As time permits**

Identical to LRB:

For: **Alvin Ott (608) 266-5831**By/Representing: **Beata Kalies**This file may be shown to any legislator: **NO**Drafter: **btradewe**

May Contact:

Addl. Drafters:

Subject: **Agriculture - miscellaneous**

Extra Copies:

Submit via email: **YES**Requester's email: **Rep.Ott@legis.state.wi.us**

Carbon copy (CC:) to:

Pre Topic:

No specific pre topic given

Topic:

Modify the agricultural producer security program

Instructions:

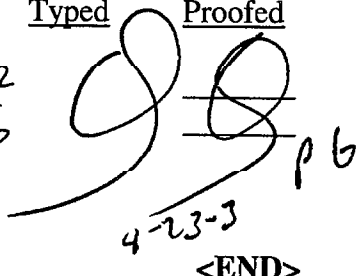
See Attached

Drafting History:

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
--------------	----------------	-----------------	--------------	----------------	------------------	-----------------	-----------------

/?

btradewe

1 q's 4/22
03

4-23-03

FE Sent For:

<END>

Bill Request Form

Legislative Reference Bureau

100 N. Hamilton Street

Legal Section 266-3561

You may use this form or talk directly with the LRB attorney who will draft the bill.

Date 3/10/03Legislator, agency, or other person requesting this draft Rep-0th / DATCPPerson submitting request (name and phone number) Beata Kalves 6-5831Persons to contact for questions about this draft (names and phone numbers) JIM MATSON 224-5022 /
ERIC HANSON 224-4968 / KEVIN LEROY 224-4928 / KEELY MOLL 224-5039

Describe the problem, including any helpful examples. How do you want to solve the problem?

Need to change the of producer security program to allow
for purchase of back up surety bonds through a line of credit.
Please see the attached preliminary draft and
supporting materials.

Please attach a copy of any correspondence or other material that may help us. If you know of any statute sections that might be affected, list them or provide a marked-up copy.

You may attach a marked-up copy of any LRB draft or provide its number (e.g., 2001 LRB-2345/1 or 1999AB-67).

Requests are confidential unless stated otherwise. May we tell others that we are working on this for you?

☒ YES ☐ NO

If yes:

Anyone who asks?

☒ YES ☐ NO

Any legislator?

☒ YES ☐ NO

Only the following persons _____

Do you consider this request urgent? ☒ YES ☐ NOIf yes, please indicate why No backup security available unless law changed to allow line of credit

Should we give this request priority over any pending request of this legislator, agency, or person?

☒ YES ☐ NO

Agricultural Producer Security

2003 Draft Legislation

1 **AN ACT to repeal** 126.07; **to renumber** 126.31(1) and 126.47(1); **to renumber and**
2 **amend** 126.31(3); **to amend** 20.115(1)(v) and (wb), 25.463, 126.05(2), 126.08,
3 126.14(2)(b)3. and 4., 126.31(8)(a)(intro.), 126.45(3)(c)3. and 4., 126.46(2)(c) and (e)
4 and (4)(c) and (c), 126.47(3)(a) and (7)(a)(intro.), 126.59(2)(c)3. and 4.,
5 126.61(1)(c)(intro.) and (7)(a)(intro.) and (b)(intro.), 126.73, 126.86(1)(g) and 126.90; **to**
6 **repeal and recreate** 126.06, 126.16(3), 126.61(3) and 126.72(2) and (3); and **to create**
7 20.115(1)(wc), 126.15(9), 126.16(1)(c) and (8)(bm), 126.30(8), 126.31(1)(b), (3)(b) and
8 (8)(am), 126.46(8), 126.47(1)(b), (3)(d) and (7)(am), 126.60(8), and 126.61(1)(bm) and
9 (7)(bm); **relating to:** agricultural producer security.

*Analysis Prepared by the Department of
Agriculture, Trade and Consumer Protection*

This bill makes a number of changes to the current agricultural producer security program under ch. 126, Stats. The program is designed to protect grain, milk and vegetable producers against financial defaults by grain dealers, grain warehouse keepers, milk contractors and vegetable contractors (collectively referred to as "contractors").

Background

The current agricultural producer security program was created, effective January 1, 2002, by 2001 Wis. Act 16. The current program replaced prior separate programs for grain, milk and vegetables. The department of agriculture, trade and consumer protection ("DATCP") administers the current program.

Prior Law

Under prior law, contractors were required to file annual financial statements with DATCP. If a contractor's financial statement failed to meet minimum financial standards (even if "just barely") the contractor was required to file individual security with DATCP. DATCP could use that security to pay producers if the operator defaulted. DATCP held over \$170 million in security from contractors who failed to meet minimum financial standards.

But under prior law, contractors who met minimum financial standards (even if "just barely") were not required to file security. If one of those operators defaulted, there was no security to pay producers. If a contractor's financial condition worsened, so that the contractor no longer met minimum financial standards, DATCP was required to demand security. Security requirements put a further strain on the contractor's financial condition, possibly increasing the contractor's risk of default.

Current Law

The current law substitutes a collective "insurance pool" for the prior program of individual security. Nearly all contractors who procure grain, milk or processing vegetables from producers must hold an annual license from DATCP and must contribute to an agricultural producer security fund (there are some exceptions). DATCP tracks fund contributions by industry (grain, milk and vegetables), but pools those contributions in a single fund.

If a contributing contractor defaults on payments to producers, DATCP may draw on the fund to compensate producers for all or part of their losses. Current law specifies a maximum *authorized payment* to each producer (the amount varies by industry). DATCP may make authorized payments from the fund, up to a maximum *deductible amount* per contractor (this amount also varies by industry).

Required fund contributions vary by industry. They also vary according to the size, financial condition and procurement practices of the contributing contractor. Other things equal, contributing contractors pay higher fund assessments if they procure large amounts of commodities, are in weak financial condition, or engage in high-risk practices. In other words, their "insurance premiums" are adjusted for risk.

The fund currently has a balance of approximately \$3.4 million. This balance is expected to grow. The current balance is already adequate to cover small and medium-sized defaults. But it is not yet adequate to cover very large defaults, or multiple defaults that might occur within a short time period.

For these situations, the current law contemplates a system of backup security. DATCP must purchase backup surety bonds to cover defaults that may exceed the capacity of the fund (bond purchase costs are payable from the fund). If DATCP makes a

demand on a surety bond, the surety company may seek repayment from the defaulting contractor but may not seek repayment from the fund.

Backup Bonds Not Currently Available

Because of current unsettled conditions in the insurance and bonding industry, DATCP has not been able to purchase the backup surety bonds contemplated by the current law (there were no bidders in response to repeated bid requests). So there is, as yet, no backup security to cover large potential defaults that may exceed the capacity of the fund.

The current law authorizes DATCP to release security filed, under prior law, by contractors who now contribute to the fund. DATCP has already released approximately \$70 million of the \$170 million in security filed under the prior law. This has reduced costs and released working capital for contributing contractors.

But because DATCP has not been able to acquire backup security for the fund, DATCP has been forced to retain much of the security filed by larger contractors under the prior law. This helps protect against defaults that might exceed the capacity of the fund. But it also imposes an unforeseen burden on the affected contractors, who must also contribute to the fund.

Maintaining the Fund

In the absence of a major default, the fund balance is expected to grow over time. DATCP may adjust fund assessments, as necessary, to maintain an appropriate balance in the fund. DATCP must consult with the agricultural producer security council before adjusting fund assessments.

DATCP may demand, from a defaulting contractor, any amount that DATCP pays out of the fund as a result of the contractor's default. But in some cases, DATCP may not be able to collect the amount owed (for example, if the defaulting contractor is bankrupt).

Bill Provisions

Alternative Backup Security

This bill authorizes DATCP to purchase a line of credit, in lieu of surety bonds, as backup security for the fund. A line of credit is more readily available, because it involves less risk for the surety company. If DATCP draws on the line of credit to pay producers victimized by a default, it must repay the loan principal and interest from the fund. DATCP may negotiate the terms with the surety company, when it purchases the line of credit. DATCP must consult with the agricultural producer security council (created under current law) before it purchases a line of credit.

DATCP may draw on the line of credit to pay producers victimized by a default, to the extent that authorized payments exceed the *deductible amount* payable from the fund. Costs to purchase the line of credit, and to repay any loan principal and interest, are payable from the fund. The state has no obligation to pay the costs from other sources.

Amount of Backup Security

Under this bill, DATCP must purchase backup security (either a surety bond or line of credit, or both) that is sufficient to cover authorized payments related to a reasonably foreseeable default. However:

- DATCP may purchase a smaller amount of backup security if, in DATCP's judgment, that is necessary to avoid excessive purchase costs or repayment liabilities for the fund.
- The amount of the backup security may not exceed \$17 million.

Security Filed By Contractors

Under current law, contractors who are disqualified from the fund must file security with DATCP. Contributing grain dealers and vegetable contractors who use "deferred payment contracts" must also file security unless they meet higher financial standards. This bill does not change these current security requirements.

DATCP also holds security filed, under prior law, by contractors who now contribute to the fund. DATCP will be able to release almost all of this security, once DATCP is able to acquire backup security for the fund.

Under this bill, a very small number of contributing contractors will still be required to file some security, even if they contribute to the fund and use no "deferred payment contracts." These are very large contractors who fail to meet minimum financial standards specified in this bill, and whose default might exceed the combined capacity of the fund and its backup security. See specific requirements for grain, milk and vegetable contractors, below.

Contributing Grain Dealers; Security

Under this bill, a grain dealer who contributes to the fund may also be required to file some security with DATCP if the grain dealer has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0. But this only applies if the grain dealer has an estimated default exposure that exceeds the following applicable amount:

- \$18 million for the license year beginning September 1, 2003.
- \$19 million for the license year beginning September 1, 2004.
- \$20 million for any subsequent license year.

A grain dealer's estimated default exposure is calculated, for this purpose, as the sum of the following:

- 35% of the grain dealer's average monthly payment for the 3 months, during the preceding 12 months, in which the grain dealer made the largest monthly payments for grain procured in this state.
- The grain dealer's highest total, at any time during the preceding 12 months, of unpaid obligations for producer grain procured in this state under deferred payment contracts.

If a contributing grain dealer is required to file security under this bill, the *amount* of security must equal the amount by which the grain dealer's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning September 1, 2003.
- \$19 million for the license year beginning September 1, 2004.
- \$20 million for any subsequent license year.

If a contributing grain dealer is required to file security under this bill, the grain dealer's annual fund assessment is reduced by a percentage that is equal to the required security amount expressed as a percentage of the grain dealer's estimated default exposure.

DATCP may release security that a contributing grain dealer is required to file under this bill if the grain dealer files 2 consecutive annual financial statements showing that the grain dealer no longer has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0.

Contributing Grain Warehouse Keepers; Security

Under this bill, a grain warehouse keeper who contributes to the fund may also be required to file some security with DATCP if the grain warehouse keeper has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0. But this only applies if the warehouse keeper's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning September 1, 2003.
- \$19 million for the license year beginning September 1, 2004.
- \$20 million for any subsequent license year.

A grain warehouse keeper's estimated default exposure is calculated, for this purpose, as 20% of the current local market value of grain that the grain warehouse keeper holds in this state for others. If a contributing grain warehouse keeper is required to file security under this bill, the *amount* of security must equal the amount by which the grain warehouse keeper's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning September 1, 2003.
- \$19 million for the license year beginning September 1, 2004.
- \$20 million for any subsequent license year.

If a contributing grain warehouse keeper is required to file security under this bill, the warehouse keeper's annual fund assessment is reduced by a percentage that is equal to the required security amount expressed as a percentage of the warehouse keeper's estimated default exposure.

DATCP may release security that a contributing grain warehouse keeper is required to file under this bill if the warehouse keeper files 2 consecutive annual financial statements showing that the warehouse keeper no longer has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0.

Contributing Milk Contractors; Security

Under this bill, a milk contractor who contributes to the fund may also be required to file some security with DATCP if the milk contractor has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 2.0 to 1.0. But this only applies if the milk contractor's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning May 1, 2003.
- \$19 million for the license year beginning May 1, 2004.
- \$20 million for any subsequent license year.

A milk contractor's estimated default exposure is calculated, for this purpose, as 75% of the largest amount of unpaid milk payroll obligations that the milk contractor had at any time during the milk contractor's last completed fiscal year. If a contributing milk contractor is required to file security under this bill, the *amount* of security must equal the amount by which the milk contractor's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning May 1, 2003.
- \$19 million for the license year beginning May 1, 2004.
- \$20 million for any subsequent license year.

If a contributing milk contractor is required to file security under this bill, the milk contractor's annual fund assessment is reduced by a percentage that is equal to the required security amount expressed as a percentage of the milk contractor's estimated default exposure.

DATCP may release security that a contributing milk contractor is required to file under this bill if the milk contractor files 2 consecutive annual financial statements showing that the milk contractor no longer has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 2.0 to 1.0.

Contributing Vegetable Contractors; Security

Under this bill, a vegetable contractor who contributes to the fund may also be required to file some security with DATCP if the vegetable contractor has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0. But this only applies if the vegetable contractor's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning February 1, 2003.
- \$19 million for the license year beginning February 1, 2004.
- \$20 million for any subsequent license year.

A vegetable contractor's estimated default exposure is calculated, for this purpose, as the sum of the following:

- 75% of the largest amount of unpaid contract obligations that the vegetable contractor had at any time during the vegetable contractor's last completed fiscal year.
- The total amount of unpaid contract obligations that the vegetable contractor has under "deferred payment contracts" (contracts payable after January 31 for vegetables harvested in the preceding calendar year).

If a contributing vegetable contractor is required to file security under this bill, the amount of security must equal the amount by which the vegetable contractor's estimated default exposure exceeds the following applicable amount:

- \$18 million for the license year beginning February 1, 2003.
- \$19 million for the license year beginning February 1, 2004.
- \$20 million for any subsequent license year.

If a contributing vegetable contractor is required to file security under this bill, the vegetable contractor's annual fund assessment is reduced by a percentage that is equal to the required security amount expressed as a percentage of the vegetable contractor's estimated default exposure.

DATCP may release security that a contributing vegetable contractor is required to file under this bill if the vegetable contractor files 2 consecutive annual financial statements showing that the vegetable contractor no longer has negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0.

Maximum Payments

If a contributing contractor defaults on payments to producers, DATCP may draw on the fund to pay all or part of the producer claims. Current law specifies a maximum authorized payment for each producer claim, depending on the type of contractor and the size of the producer's claim. DATCP may make the authorized payments from the fund, up to a maximum aggregate amount (deductible amount) for all producer claims against the contractor. DATCP must draw on backup security to make the balance of the authorized payments. Current law specifies the following deductible amounts:

- For default claims against a grain dealer or grain warehouse keeper who was a "contributing contractor" when the default occurred:
 - \$500,000 if DATCP allows the claims on or after September 1, 2002 but before September 1, 2004.
 - \$750,000 if DATCP allows the claims on or after September 1, 2004 but before September 1, 2006.
 - \$1 million if DATCP allows the claims on or after September 1, 2006.
- For default claims against a milk contractor who was a "contributing contractor" when the default occurred:
 - \$1 million if DATCP allows the claims on or after May 1, 2002 but before May 1, 2004.
 - \$1.5 million if DATCP allows the claims on or after May 1, 2004 but before May 1, 2006.
 - \$2 million if DATCP allows the claims on or after May 1, 2006.
- For default claims against a vegetable contractor who was a "contributing contractor" when the default occurred:
 - \$500,000 if DATCP allows the claims on or after February 1, 2002 but before September 1, 2004.
 - \$750,000 if DATCP allows the claims on or after February 1, 2004 but before September 1, 2006.
 - \$1 million if DATCP allows the claims on or after February 1, 2006.

This bill repeals these current deductible amounts, and specifies a new uniform deductible amount for all contractor defaults. The new uniform deductible amount is 60% of the cash balance in the fund on the last day of the month preceding the date of the default.

How much more \$ would it be + for which contractors?

There would be an increase more down the road as the fund grows...

40% retained

Helps line of credit - would give money more easily

(the new 60% of fund balance)

Start-up Loan to Fund; Repayment

When the Legislature created the agricultural producer security fund effective January 1, 2002, it established an initial fund balance of \$2 million by transferring that amount as a loan from the agrichemical management fund. DATCP must repay the \$2 million principal, plus interest, from the agricultural producer security fund by July 1, 2006. DATCP must repay at least \$250,000 each year but may accelerate the loan repayment, at its discretion. Under current law, interest on the loan is compounded at 5% annually. This bill changes the current interest rate. Under this bill, interest is compounded at 5% annually until July 1, 2003 and at 2% annually beginning on July 1, 2003.

Other Changes to Current Law

This bill makes other minor changes to current law. Among other things, this bill clarifies current provisions related to fund assessments paid by producer agents. These clarifications do not change the way that DATCP has interpreted and applied the law to date.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

- 1 ✓ SECTION 1. 20.115(1)(v) of the statutes is amended to read:
- 2 20.115(1)(v) *Agricultural producer security; ~~bonds~~ contingent financial backing.*
- 3 From the agricultural producer security fund, a sum sufficient to acquire the ~~surety bonds~~
- 4 contingent financial backing required under ~~ss. s.~~ s. 126.06 and 126.07.
- 5 ✓ SECTION 2. 20.115(1)(wb) of the statutes is amended to read:
- 6 20.115(1)(wb) *Agricultural producer security; ~~bond proceeds~~ contingent*
- 7 financial backing. From the agricultural producer security fund, all moneys received
- 8 under s. 126.72(2) ~~and (3)~~ to be used to make default claim payments under s. 126.71(1).
- 9 ✓ SECTION 3. 20.115(1)(wc) of the statutes is created to read:
- 10 20.115(1)(wc) *Agricultural producer security; contingent financial backing.*
- 11 From the agricultural producer security fund, a sum sufficient to repay obligations arising
- 12 from the use of contingent financial backing under s. 126.06(1)(b).

1 ✓ **SECTION 4.** 25.463 of the statutes is amended to read:

2 **25.463 Agricultural producer security fund.** There is established a separate
3 nonlapsible trust fund designated as the agricultural producer security fund, to consist of
4 all fees, surcharges, assessments, reimbursements and proceeds of ~~surety bonds~~
5 contingent financial backing received by the department of agriculture, trade and
6 consumer protection under ch. 126.

7 ✓ **SECTION 5.** 126.05(2) of the statutes is amended to read:

8 126.05(2) The department shall deposit into the fund all fees, surcharges,
9 assessments, reimbursements, and proceeds of ~~surety bonds~~ contingent financial backing
10 that the department collects under this chapter. The department shall keep a record by
11 contractor and industry, of all deposits.

12 ✓ **SECTION 6.** 126.06 of the statutes is repealed and recreated to read:

13 **126.06 Contingent financial backing.** (1) DEPARTMENT TO ACQUIRE
14 CONTINGENT FINANCIAL BACKING. Using moneys appropriated under s. 20.115(1)(v), the
15 department shall acquire contingent financial backing to secure payment under s.
16 126.72(2) of claims against contributing contractors, as defined in s. 126.68(1). The
17 contingent financial backing may be in one or more of the following forms:

18 (a) A surety bond.

19 (b) A contract to provide a cash loan to the fund, if and when the department
20 requests that loan to the fund. Loan repayments and interest charges, if any, are payable
21 from the fund pursuant to the appropriation in s. 20.115(1)(wc).

1 (2) AMOUNT. The amount of the contingent financial backing under sub. (1)
2 shall be sufficient, in the department's judgment, to meet reasonably foreseeable needs
3 under s. 126.72(2) except that:

4 (a) The department may acquire a smaller amount of contingent financial backing
5 if, in the department's judgment, that is necessary to avoid excessive acquisition costs or
6 repayment liabilities.

7 (b) The amount of the contingent financial backing may not exceed \$17 million. *

8 ✓ SECTION 7. 126.07 of the statutes is repealed.

9 SECTION 8. 126.08 of the statutes is amended to read:

10 ✓ 126.08 Start-up loan to fund; repayment. On January 1, 2002, \$2,000,000 is
11 transferred as a loan from the agrichemical management fund, to the agricultural
12 producer security fund. The department shall repay this loan principal, plus interest
13 ~~compounded at 5% annually~~, from the agricultural producer security fund by July 1,
14 2006. Interest shall be compounded at 5% annually until July 1, 2003 and at 2% annually
15 beginning on July 1, 2003. The department shall transfer at least \$250,000 from the
16 agricultural producer security fund to the agrichemical management fund on July 1 of
17 each year, beginning on July 1, 2003. The department may accelerate the loan repayment
18 at its discretion.

19 ✓ SECTION 9. 126.14(2)(b)3. and 4. of the statutes are amended to read:

20 126.14(2)(b)3. The grain dealer fails to reimburse the department, within 60 days
21 after the department issues a demand under s. 126.73(1), for the full amount that the
22 department pays to claimants under s. 126.72(1) or (2) because of that grain dealer's
23 default.

*unless otherwise
amended by Dpty
rules.*

1 (b)4. The grain dealer fails to reimburse a bond surety, within 60 days after the
2 bond surety issues a reimbursement demand under s. 126.73(2), for the full amount that
3 the surety pays to the department under s. 126.72(2) ~~or (3)~~ for the benefit of claimants
4 affected by that grain dealer's default.

5 SECTION 10. 126.15(9) is created to read:

6 126.15(9) REDUCED ASSESSMENT FOR GRAIN DEALERS FILING SECURITY. If a
7 grain dealer files security under s. 126.16(1)(c), the grain dealer's assessment under sub.
8 (1) is reduced by a percentage that is equal to the amount under s. 126.16(3)(b) expressed
9 as a percentage of the total amount under s. 126.16(3)(a).

10 SECTION 11. 126.16(1)(c) is created to read:

11 126.16(1)(c) A grain dealer shall file security with the department, and maintain
12 that security until the department releases it under sub. (8)(bm), if the grain dealer files an
13 annual financial statement under s. 126.13(1)(a) that shows negative equity, a current
14 ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to 1.0. This
15 paragraph does not apply if the total amount under sub. (3)(a) is less than the following
16 applicable amount:

- 17 1. \$18 million for the license year beginning September 1, 2003.
18 2. \$19 million for the license year beginning September 1, 2004.
19 3. \$20 million for the license years beginning September 1, 2005 or later.

20 SECTION 12. 126.16(3) of the statutes is repealed and recreated to read:

21 126.16(3) AMOUNT OF SECURITY. (a) Except as provided in par. (b), a grain
22 dealer who is required to file or maintain security under this section shall, at all times,
23 maintain security that is at least equal to the sum of the following:

1 1. Thirty-five percent of the grain dealer's average monthly payment for the 3
2 months, during the preceding 12 months, in which the grain dealer made the largest
3 monthly payments for producer grain procured in this state. This amount does not apply
4 to a contributing contractor, except for purposes of par. (b) and sub. (1)(c).

5 2. The grain dealer's highest total, at any time during the preceding 12 months, of
6 unpaid obligations for producer grain procured under deferred payment contracts.

7 (b) A grain dealer who is only required to file or maintain security under sub.
8 (1)(c) shall at all times maintain security equal to the total amount in par. (a) less the
9 following applicable amount:

10 1. \$18 million for the license year beginning September 1, 2003.

11 2. \$19 million for the license year beginning September 1, 2004.

12 3. \$20 million for the license years beginning September 1, 2005 or later.

13 SECTION 13. 126.16(8)(bm) of the statutes is created to read:

14 126.16(8)(bm) The department may release security filed under sub. (1)(c),
15 except for any amount of security that the grain dealer is required to file because sub.
16 (1)(a) or (b) applies to the grain dealer, if the grain dealer files 2 consecutive annual
17 financial statements under s. 126.13 showing that the grain dealer no longer has negative
18 equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to
19 1.0.

20 SECTION 14. 126.30(8) is created to read:

21 126.30(8) REDUCED ASSESSMENT FOR GRAIN WAREHOUSE KEEPER FILING
22 SECURITY. If a grain warehouse keeper files security under s. 126.31(1)(b), the grain
23 warehouse keeper's assessment under sub. (1) is reduced by a percentage that is equal to

1 the amount under s. 126.31(3)(b) expressed as a percentage of the amount under s.
2 126.31(3)(a).

3 SECTION 15. 126.31(1) of the statutes is renumbered (1)(a).

4 SECTION 16. 126.31(1)(b) of the statutes is created to read:

5 126.31(1)(b) A grain warehouse keeper shall file security with the department,
6 and maintain that security until the department releases it under sub. (8)(am), if the grain
7 warehouse keeper files an annual financial statement under s. 126.28(1)(a) that shows
8 negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more
9 than 4.0 to 1.0. This paragraph does not apply if the amount under sub. (3)(a) is less than
10 the following applicable amount:

- 11 1. \$18 million for the license year beginning September 1, 2003.
- 12 2. \$19 million for the license year beginning September 1, 2004.
- 13 3. \$20 million for the license years beginning September 1, 2005 or later.

14 SECTION 17. 126.31(3) of the statutes is renumbered (3)(a) and amended to read:

15 126.31(3)(a) A Except as provided in par. (b), a grain warehouse keeper who is
16 required to file or maintain security under this section shall at all times maintain security
17 equal to at least 20% of the current local market value of grain that the grain warehouse
18 keeper holds in this state for others.

19 SECTION 18. 126.31(3)(b) of the statutes is created to read:

20 126.31(3)(b) A grain warehouse keeper who is only required to file or maintain
21 security under sub. (1)(b) shall at all times maintain security equal to the amount in par.
22 (a) less the following applicable amount:

- 23 1. \$18 million for the license year beginning September 1, 2003.

1 2. \$19 million for the license year beginning September 1, 2004.

2 3. \$20 million for the license years beginning September 1, 2005 or later.

3 SECTION 19. 126.31(8)(a)(intro.) of the statutes is amended to read:

4 126.31(8)(a)(intro.) The department may release security filed under ~~sub. (1)~~ sub.

5 (1)(a) if any of the following applies:

6 SECTION 20. 126.31(8)(am) of the statutes is created to read:

7 126.31(8)(am) The department may release security filed under sub. (1)(b),

8 except for any amount of security that the grain warehouse keeper is required to file

9 because sub. (1)(a) applies to the grain warehouse keeper, if the grain warehouse keeper

10 files 2 consecutive annual financial statements under s. 126.28 showing that the grain

11 warehouse keeper no longer has negative equity, a current ratio of less than 1.25 to 1.0, or

12 a debt to equity ratio of more than 4.0 to 1.0.

13 ✓ SECTION 21. 126.45(3)(c)3. and 4. of the statutes are amended to read:

14 126.45(3)(c)3. Failure to reimburse the department, within 60 days after the

15 department issues a reimbursement demand under s. 126.73(1), for the full amount that

16 the department pays to claimants under s. 126.72(1) or (2) because of that milk

17 contractor's default.

18 (c)4. Failure to reimburse a bond surety, within 60 days after the bond surety

19 issues a reimbursement demand under s. 126.73(2), for the full amount that the surety

20 pays to the department under s. 126.72(2) ~~or (3)~~ for the benefit of claimants affected by

21 that milk contractor's default.

22 ✓ SECTION 22. 126.46(2)(c) and (e) of the statutes are amended to read:

1 126.46(2)(c). If Except as provided in par. (e), if the milk contractor has filed an
2 annual financial statement under s. 126.44 and that financial statement shows a current
3 ratio less than or equal to 1.05 to 1.0, the milk contractor's current ratio assessment rate
4 equals the current ratio assessment factor in sub. (3)(b) multiplied by 0.1201478.

5 (2)(e) If the milk contractor ~~has not filed an annual financial statement under s.~~
6 ~~126.44 and the milk contractor~~ procures producer milk in this state solely as a producer
7 agent, and the milk contractor has not filed an annual financial statement under s. 126.44
8 or has filed a financial statement that shows a current ratio of less than 1.05 to 1.0, the
9 milk contractor's current ratio assessment rate is 0.00025; except that, for the milk
10 contractor's 5th or higher consecutive full license year of participation in the fund, the
11 milk contractor's current ratio assessment rate is 0.000175.

12 ✓ SECTION 23. 126.46(4)(c) and (e) of the statutes are amended to read:

13 126.46(4)(c). If Except as provided in par. (e), if the milk contractor has filed an
14 annual financial statement under s. 126.44 and that financial statement shows negative
15 equity or a debt to equity ratio of at least 3.1 to 1.0, the milk contractor's debt to equity
16 ratio assessment rate equals the debt to equity ratio assessment factor in sub. (5)(b)
17 multiplied by 0.8146917.

18 (4)(e). If the milk contractor ~~has not filed an annual financial statement under s.~~
19 ~~126.44 and the milk contractor~~ procures producer milk in this state solely as a producer
20 agent, and the milk contractor has not filed an annual financial statement under s. 126.44
21 or has filed a financial statement that shows negative equity or a debt to equity ratio of at
22 least 3.1 to 1.0, the milk contractor's debt to equity ratio assessment rate is 0.00025,
23 except that, for the milk contractor's 5th or higher consecutive full license year of

1 participation in the fund, the milk contractor's debt to equity ratio assessment rate is
2 0.000175.

3 **SECTION 24.** 126.46(8) is created to read:

4 126.46(8) REDUCED ASSESSMENT FOR MILK CONTRACTOR FILING SECURITY. If a
5 milk contractor files security under s. 126.47(1)(b), the milk contractor's assessment
6 under sub. (1) is reduced by a percentage that is equal to the amount in s. 126.47(3)(d)
7 expressed as a percentage of the amount in s. 126.47(3)(a).

8 **SECTION 25.** 126.47(1) of the statutes is renumbered (1)(a).

9 **SECTION 26.** 126.47(1)(b) of the statutes is created to read:

10 126.47(1)(b) A milk contractor shall file security with the department, and
11 maintain that security until the department releases it under sub. (7)(am), if the milk
12 contractor files an annual financial statement under s. 126.44(1) that shows negative
13 equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 2.0 to
14 1.0. This paragraph does not apply if 75% of the amount last reported under s.
15 126.41(6)(b) or (9) is less than the following applicable amount:

- 16 1. \$18 million for the license year beginning May 1, 2003.
- 17 2. \$19 million for the license year beginning May 1, 2004.
- 18 3. \$20 million for the license years beginning May 1, 2005 or later.

19 **SECTION 27.** 126.47(3)(a) of the statutes is amended to read:

20 126.47(3)(a) Except as provided in ~~par. (b) or (c)~~ pars. (b) to (d), security equal to
21 at least 75% of the amount last reported under s. 126.41(6)(b) or (9).

22 **SECTION 28.** 126.47(3)(d) of the statutes is created to read:

1 126.47(3)(d) A milk contractor who is only required to file or maintain security
2 under sub. (1)(b) shall at all times maintain security equal to the amount in par. (a) less
3 the following applicable amount:

- 4 1. \$18 million for the license year beginning May 1, 2003.
- 5 2. \$19 million for the license year beginning May 1, 2004.
- 6 3. \$20 million for the license years beginning May 1, 2005 or later.

7 SECTION 29. 126.47(7)(a)(intro.) of the statutes is amended to read:

8 126.47(7)(a)(intro.) The department may release security filed under ~~sub. (1)~~ sub.
9 (1)(a) if any of the following applies:

10 SECTION 30. 126.47(7)(am) of the statutes is created to read:

11 126.47(7)(am) The department may release security filed under sub. (1)(b),
12 except for any amount of security that the milk contractor is required to file because sub.
13 (1)(a) applies to the milk contractor, if the milk contractor files 2 consecutive annual
14 financial statements under s. 126.44 showing that the milk contractor no longer has
15 negative equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more
16 than 2.0 to 1.0.

17 SECTION 31. 126.59(2)(c)3. and 4. are amended to read:

18 126.59(2)(c)3. Failure to reimburse the department, with 60 days after the
19 department issues a reimbursement demand under s. 126.73(1), for the full amount that
20 the department pays to claimants under s. 126.72(1) or (2) because of that vegetable
21 contractor's default.

22 (c)4. Failure to reimburse a bond surety, within 60 days after the bond surety
23 issues a reimbursement demand under s. 126.73(2), for the full amount that the surety

1 pays to the department under s. 126.72(2) ~~or (3)~~ for the benefit of claimants affected by
2 that vegetable contractor's default.

3 SECTION 32. 126.60(8) is created to read:

4 126.60(8) REDUCED ASSESSMENT FOR VEGETABLE CONTRACTOR FILING SECURITY.

5 If a vegetable contractor files security under s. 126.61(1)(bm), the vegetable contractor's
6 assessment under sub. (1) is reduced by a percentage that is equal to the amount in s.
7 126.61(3)(b) expressed as a percentage of the total amount in s. 126.61(3)(a).

8 SECTION 33. 126.61(1)(bm) of the statutes is created to read:

9 126.61(1)(bm) A vegetable contractor shall file security with the department, and
10 maintain that security until the department releases it under sub. (7)(bm), if the vegetable
11 contractor files an annual financial statement under s. 126.58(1)(b) that shows negative
12 equity, a current ratio of less than 1.25 to 1.0, or a debt to equity ratio of more than 4.0 to
13 1.0. This paragraph does not apply if the vegetable contractor is exempt under par. (c) or
14 if the total amount in sub. (3)(a) is less than the following applicable amount:

- 15 1. \$18 million for the license year beginning February 1, 2003.
- 16 2. \$19 million for the license year beginning February 1, 2004.
- 17 3. \$20 million for a license year beginning February 1, 2005 or later.

18 SECTION 34. 126.61(1)(c)(intro.) is amended to read:

19 126.61(1)(c)(intro.) A vegetable contractor is not required to file security under
20 ~~par. (a) or (b)~~ this subsection if any of the following apply:

21 SECTION 35. 126.61(3) of the statutes is repealed and recreated to read:

1 126.61(3) AMOUNT OF SECURITY. (a) Except as provided in par. (b), a vegetable
2 contractor who is required to file or maintain security under this section shall, at all times,
3 maintain security that is at least equal to the sum of the following:

4 1. Seventy-five percent of the amount last reported under s. 126.56(9)(b) or
5 (12)(a). This amount does not apply to a contributing contractor, except for purposes of
6 par. (b) and sub. (1)(bm).

7 2. The amount required under sub. (1)(b), if any.

8 (b) A vegetable contractor who is only required to file or maintain security under
9 sub. (1)(bm) shall at all times maintain security equal to the total amount in par. (a) less
10 the following applicable amount:

11 1. \$18 million for the license year beginning February 1, 2003.

12 2. \$19 million for the license year beginning February 1, 2004.

13 3. \$20 million for the license years beginning February 1, 2005 or later.

14 SECTION 36. 126.61(7)(a)(intro.) of the statutes is amended to read:

15 126.61(7)(a)(intro.) The department may release security filed under sub. (1)(a),
16 except for any amount of security that the vegetable contractor is required to file because
17 sub. (1)(b) or (bm) applies to the vegetable contractor, if any of the following applies:

18 SECTION 37. 126.61(7)(b)(intro.) of the statutes is amended to read:

19 126.61(7)(b)(intro.) The department may release security filed under sub. (1)(b),
20 except for any amount of security that the vegetable contractor is required to file because
21 sub. (1)(a) or (bm) applies to the vegetable contractor, if any of the following applies:

22 SECTION 38. 126.61(7)(bm) of the statutes is created to read:

1 126.61(7)(bm) The department may release security filed under sub. (1)(bm),
2 except for any amount of security that the vegetable contractor is required to file because
3 sub. (1)(a) or (b) applies to the vegetable contractor, if the vegetable contractor files 2
4 consecutive annual financial statements under s. 126.58 showing that the vegetable
5 contractor no longer has negative equity, a current ratio of less than 1.25 to 1.0, or a debt
6 to equity ratio of more than 4.0 to 1.0.

7 **SECTION 39.** 126.72(2) and (3) of the statutes are repealed and recreated to read:

8 126.72(2) CONTINGENT FINANCIAL BACKING. The department shall draw on the
9 contingent financial backing acquired under s. 126.06 to make payments authorized
10 under s. 126.71(1), to the extent that those payments exceed the deductible amount in
11 sub. (3).

12 (3) DEDUCTIBLE AMOUNT. The deductible amount, for purposes of subs. (1) and
13 (2), is equal to 60% of the cash balance in the agricultural producer security fund on the
14 last day of the month preceding the date of the default.

15 **SECTION 40.** 126.73 of the statutes is amended to read:

16 **126.73 Reimbursing payments. (1) PAYMENTS FROM THE FUND.** The
17 department may demand and collect, from a contractor, any claim amounts that the
18 department pays from the fund or with the proceeds of contingent financial backing under
19 s. 126.72(1) or (2) because of the contractor's default.

20 (2) BOND PAYMENTS. A bond surety may demand and collect, from a contractor,
21 any claim amounts that the bond surety pays to the department under s. 126.72(2) ~~or (3)~~
22 because of the contractor's default. The bond surety shall provide the department with a
23 copy of each demand under this subsection.

SECTION 41. 126.86(1)(g) of the statutes is amended to read:

126.86(1)(g) The contractor fails to reimburse a bond surety, within 60 days after the bond surety issues a reimbursement demand under s. 126.73(2), for the full amount that the surety pays to the department under s. 126.72(2) ~~or (3)~~ for the benefit of claimants affected by the contractor's default.

SECTION 42. 126.90 of the statutes is amended to read:

126.90 Agricultural producer security council. The agricultural producer security council shall advise the department on the administration and enforcement of this chapter. The council shall meet as often as necessary, but at least once annually. The department shall inform the council of fund balances and payments, and, The department shall consult with the council before acquiring any contingent financial backing under s. 126.06, and before modifying any license fee, license surcharge, or fund assessment under this chapter.

(END)



State of Wisconsin
Jim Doyle, Governor

Department of Agriculture, Trade and Consumer Protection
Rod Nilsestuen, Secretary

DATE: February 14, 2003

TO: Board of Agriculture, Trade and Consumer Protection

FROM: *h* Rodney J. Nilsestuen, Secretary
Eric Hanson, Agricultural Producer Security Section *EJH*

SUBJECT: Agricultural Producer Security Legislation

At the February 26, 2003 Board meeting, the department will present preliminary draft legislation (copy attached) to modify the agricultural producer security program under ch. 126, Stats. The department will not ask the Board to endorse this specific draft bill on February 26, but will seek general Board direction on a continued legislative effort.

The agricultural producer security program is designed to protect grain, milk and vegetable producers against catastrophic financial defaults by grain dealers, grain warehouse keepers, milk contractors and vegetable contractors (collectively known as "contractors" under ch. 126, Stats.). The program helps secure approximately \$10 billion in contractor payments to producers each year. A contractor's default can have a devastating impact on agricultural producers, not unlike a bank failure.

The Legislature completely overhauled the agricultural producer security program, effective January 1, 2002. To date, contractors and producer groups have expressed strong overall support for the new program, which provides better protection to producers at lower cost to contractors. But unforeseen changes in the insurance and bonding industry (related to September 11 and other events) have forced the department to reconsider some parts of the new program. The department has prepared this draft bill to address some remedial changes that may be needed.

On February 25, 2002, the department plans to discuss this draft bill with the Agricultural Producer Security Council, which represents affected producers and contractors (see membership list attached). The council supports this legislative effort in principle, but has not yet reviewed the specific provisions of this bill. This bill has not yet been introduced in the Legislature, although several legislators have expressed interest in it. Before any bill can be introduced in the Legislature, it must undergo final drafting by the Legislative Reference Bureau.

Background

The current agricultural producer security program was created, effective January 1, 2002, by 2001 Wis. Act 16. The current program replaced prior separate programs for grain, milk and vegetables. The department of agriculture, trade and consumer protection ("DATCP") administers the current program.

Prior Law: "All or Nothing" Security

Under prior law, contractors were required to file annual financial statements with DATCP. If the contractor's financial statement failed to meet minimum financial standards (even if "just barely"), the contractor was required to file individual security with DATCP. DATCP could use that security to pay producers if the operator defaulted. Under the prior law, DATCP held over \$170 million in security from contractors who failed to meet minimum financial standards. This represented a very large cost for many contractors.

At the same time, contractors who met minimum financial standards (even if "just barely") were *not* required to file security. If one of those operators defaulted, there was no security to pay producers. If a contractor's financial condition worsened, so that the contractor could no longer meet minimum financial standards, DATCP was required to demand security. Security requirements put further strain on the contractor's financial condition, possibly increasing the contractor's risk of default.

Individual security filings were costly to the industry, and deprived contractors of needed working capital. Security filings could not keep pace with volatile commodity price changes, which affected the amount of security needed. Some forms of security, authorized under prior law, were also unworkable in practice. As a result, producer payments were sometimes delayed for years.

Current Law: Indemnity Fund and Backup Bonds

The current law substitutes a collective "insurance pool" for the prior "all or nothing" program of individual security. Nearly all contractors who procure grain, milk or processing vegetables from producers must hold an annual license from DATCP and must contribute to an agricultural producer security fund (there are some exceptions). DATCP tracks fund contributions by industry (grain, milk and vegetables), but pools those contributions in a single fund.

If a contributing contractor defaults on payments to producers, DATCP may draw on the fund to compensate producers for all or part of their losses. Current law specifies a maximum *authorized payment* to each producer (the amount varies by industry). DATCP may make the authorized payments from the fund, up to a maximum *deductible amount* per contractor (this amount also varies by industry).

Required fund contributions vary by industry. They also vary according to the size, financial condition and procurement practices of the contributing contractor. Other things equal, contributing contractors pay higher fund assessments if they procure large amounts of commodities, are in weak financial condition, or engage in high-risk practices. In other words, their "insurance premiums" are adjusted for risk.

The fund currently has a balance of approximately \$3.4 million. This balance is expected to grow. The current balance is already adequate to cover small and medium-sized defaults (the largest default to date was the \$2.5 million Kasson Cheese default). But the balance is not yet adequate to cover very large defaults, or multiple defaults that might occur within a short time period.

For these situations, the current law contemplates a system of backup security. DATCP must purchase backup surety bonds to cover defaults that may exceed the capacity of the fund (bond purchase costs are payable from the fund). If DATCP makes a demand on a surety bond, the surety company may seek repayment from the defaulting contractor, but may not seek repayment from the fund.

Backup Bonds Not Currently Available

Because of current unsettled conditions in the insurance and bonding industry, DATCP has not been able to purchase the required backup surety bonds (there were no bidders in response to repeated bid requests). So there is, as yet, no backup security to cover large potential defaults that may exceed the capacity of the fund.

The current law authorizes DATCP to release security filed, under prior law, by contractors who now contribute to the fund. DATCP has already released approximately \$70 million of the \$170 million in security filed under the prior law. This has reduced costs and released working capital for contributing contractors.

But because DATCP has not been able to acquire backup security for the fund, DATCP has been forced to retain much of the security filed by larger contractors under the prior law. This helps protect against defaults that might exceed the capacity of the fund. But it also imposes an unforeseen burden on the affected contractors, who must also contribute to the fund.

Maintaining the Fund

In the absence of a major default, the fund balance is expected to grow over time. Eventually, this will reduce the need for backup security. DATCP may adjust fund assessments to maintain an appropriate balance in the fund. DATCP must consult with the Agricultural Producer Security Council before adjusting fund assessments.

DATCP may demand, from a defaulting contractor, any amount that DATCP pays out of the fund as a result of the contractor's default. But in some cases, DATCP may not be able to collect the amount owed (for example, if the defaulting contractor is bankrupt).

Contents of this Draft Legislation

Alternative Backup Security

This bill authorizes DATCP to purchase a line of credit, in lieu of surety bonds, as backup security for the fund. A line of credit is more readily available, because it involves less risk for the surety company. If DATCP draws on the line of credit to pay producers victimized by a default, it must repay the loan principal and interest from the fund. DATCP may negotiate the terms with the surety company, when it purchases the line of credit. DATCP must consult with the agricultural producer security council (created under current law) before it purchases a line of credit.

DATCP may draw on the line of credit to pay producers victimized by a default, to the extent that the authorized payments exceed the *deductible amount* payable from the fund. If DATCP draws on the line of credit, DATCP must repay the loan principal and interest from the fund. Costs to purchase the line of credit, and to repay any loan principal and interest, are payable from the fund. The state has no obligation to pay the costs from other sources.

Amount of Backup Security

Under this bill, DATCP must purchase backup security (either a surety bond or line of credit, or both) that is sufficient to cover authorized payments related to a reasonably foreseeable default. However:

- DATCP may purchase a smaller amount of backup security if, in DATCP's judgment, that is necessary to avoid excessive purchase costs or repayment liabilities for the fund.
- The amount of the backup security may not exceed \$17 million.

Releasing Security Filed by Individual Contractors

If DATCP obtains a line of credit, as authorized by this bill, DATCP will be able to release nearly all of the security filed (under prior law) by contractors who now contribute to the fund. A very small number of contributing contractors will still be required to keep *some* individual security on file (less than currently), if they fail to meet minimum financial standards prescribed in this bill. These are very large contractors whose default would exceed the *combined* capacity of the fund *and* the new backup security. These contractors would be compensated, in part, by a reduction in their fund assessments. The bill spells out specific security requirements and fund assessment adjustments for grain, milk and vegetable contractors.

Maximum Payment from Fund

If a contractor defaults in payments to producers, DATCP may draw on the fund to compensate producers for all or part of their losses. Current law specifies a maximum *authorized payment* for each producer claim, depending on the type of contractor and the size of the producer's claim. DATCP may make the authorized payments from the fund, up to a maximum aggregate amount (*deductible amount*) for all producer claims against the contractor. DATCP must draw on backup security to make the balance of the authorized payments.

The current law specifies different *deductible amounts* for the different industries (grain, milk and vegetables). These amounts increase over time as the fund balance grows. This bill repeals the current deductible amounts, and specifies a new uniform deductible amount for all contractor defaults. The new uniform deductible amount is 60% of the cash balance in the fund on the last day of the month preceding the date of the default.

Start-up Loan to Fund; Repayment

When the Legislature created the agricultural producer security fund effective January 1, 2002, it established an initial fund balance of \$2 million by transferring that amount as a loan from the agrichemical management fund. DATCP must repay the \$2 million principal, plus interest, from the agricultural producer security fund by July 1, 2006. DATCP must repay at least \$250,000 each year but may accelerate the loan repayment, at its discretion. Under current law, interest on the loan is compounded at 5% annually. This bill changes the current interest rate. Under this bill, interest is compounded at 5% annually until July 1, 2003 and at 2% annually beginning on July 1, 2003.

Agricultural Producer Security Council

Appointed Individuals

First Name	Last Name	Title	Company	Representing
Gary	Braun	Director of Agriculture/Production Services	Del Monte Foods	Midwest Food Processors Association, Inc.
Mike	Carter	Director of Government and Grower Relations <i>Exec. Dir.</i>	Wisconsin Potato & Vegetable Growers Assoc.	Wisconsin Potato & Vegetable Growers Association, Inc.
Dave	Daniels			Wisconsin Farm Bureau Federation
Richard	Keller			Farmers' Educational and Cooperative Union of America, Wisconsin Division
John	Manske	Director of Governmental Relations	Wisconsin Federation of Cooperatives	Wisconsin Federation of Cooperatives
John	Petty	Executive Director	Wisconsin Agri-Service Association	Wisconsin Agri-Service Association, Inc.
Doug	Simon	Executive Vice President	Weyauwega Milk Products, Inc.	Wisconsin Cheese Makers Association
Ron	Statz	Membership Services Director	Wisconsin NFO	Wisconsin National Farmers Organization, Inc.
Ed	Welch	General Manager	AMPI North Central	Wisconsin Dairy Products Association, Inc.
Jim	Zimmerman			Wisconsin Corn Growers Association and the Wisconsin Soybean Association

2-25-03

Department of Agriculture, Trade and Consumer Protection

State Backup Security for the Agricultural Producer Security Fund?

The Department of Agriculture, Trade and Consumer Protection (DATCP) administers the agricultural producer security program under ch. 126, Stats. The program protects agricultural producers against catastrophic defaults by grain dealers, grain warehouse keepers, milk contractors and vegetable contractors (collectively known as "contractors"). In the event of a default, DATCP may reimburse producers from an agricultural producer security fund financed by contractor assessments. If the default exceeds the capacity of the fund, DATCP may resort to backup security.

The current law requires DATCP to obtain backup security in the form of surety bonds issued by private surety companies. However, there are no surety companies currently willing to provide such bonds. DATCP is proposing legislation that would authorize DATCP to obtain a "line of credit" in lieu of surety bonds. A "line of credit" is more readily available, because it involves less risk for the surety company. DATCP would purchase a guaranteed "line of credit" with money from the agricultural producer security fund. In the event of a default, DATCP could immediately draw on the "line of credit" to pay producer claims that exceed the capacity of the fund. DATCP would repay the loan amount, with interest, from the fund.

At the request of the Agricultural Producer Security Council, DATCP has investigated the possibility of state-financed backup funding for the agricultural producer security fund (in lieu of a surety bond or line of credit, as contemplated by the DATCP's draft legislation). DATCP has investigated the alternatives identified in this memo, and has found no readily available state funding mechanisms at this time.

Public Funding Alternatives

1. Fund Backed by GPR (General Tax Dollars)

- **Description.** Under this alternative, the state would pay the balance of any default claims not covered by the agricultural producer security fund. Payments would be financed by state GPR funds (general tax dollars). Budget legislation would provide a "sum sufficient" GPR appropriation (whatever is needed to cover defaults that exceed the capacity of the fund).
- **Problem.** This alternative would expose the state treasury to large, unpredictable financial obligations. The state already has a large projected GPR deficit, so there is no GPR funding available for this purpose.

2. Backup Loans Funded by GPR

- **Description.** Under this alternative, the state would provide sum sufficient GPR funding for emergency loans to the agricultural producer security fund. DATCP could use the loans to pay default claims that exceed the capacity of the agricultural producer security fund. The agricultural producer security fund would repay the loans, with interest. Budget legislation would provide a "sum sufficient" GPR appropriation (whatever is needed to make required emergency loans).
- **Problem.** This alternative would expose the state treasury to large, unpredictable financial obligations (although the agricultural producer security fund would eventually repay the obligations with interest). The state already has a large projected GPR deficit, so there is no GPR funding available for this purpose.

3. Backup Loans Funded by State General Obligation Bonds

- **Description.** Under this alternative, the state would fund backup loans to the agricultural producer security fund. DATCP could draw on this funding to pay producers if there were a default exceeding the capacity of the fund. The state would issue general obligation bonds to finance the loans. The state would repay the general obligation bonds with interest, from the general fund. The agricultural producer security fund would repay the general fund.
- **Problem.** This alternative is probably unconstitutional. Under the state constitution, the state may only issue general obligation bonds (re-payable from the general fund) for capital improvements having a public purpose. Default payments to individual producers under the agricultural producer security program do not constitute "capital improvements" and may not satisfy the "public purpose" test.

4. Backup Loans Funded by WHEDA Bonds

- **Description.** Under this alternative, the Wisconsin Housing and Economic Development Authority (WHEDA) would issue bonds to finance backup loans to the agricultural producer security fund. DATCP could request a loan to pay producers victimized by a default that exceeded the capacity of the fund. WHEDA would sell bonds, and lend the bond proceeds to DATCP. The agricultural producer security fund would repay the bond amount, with interest. The state treasury would not be obligated on the bond, and would not be liable for any bond payment.

- **Problem.** This alternative might avoid the constitutional problem associated with state general obligation bonds (because it creates no liability for the state itself). But it would require special legislation. The Legislature would need to decide whether it is appropriate, and constitutionally permissible, to use WHEDA bonding authority for this purpose. Even if the Legislature granted authorization, there could be many problems.

WHEDA currently sells bonds to finance loans for capital improvements, identified in ch. 234, Stats., that have an important public purpose (economic development, low income housing, etc.). The borrower repays the bond principal and interest, under an arrangement with WHEDA. The bond purchaser typically holds a mortgage or security interest in the borrower's enterprise, to secure payment. Because interest on WHEDA bonds is exempt from income taxation, interest rates may be lower than normal market rates.

The agricultural producer security program is different from other programs financed by WHEDA. Its borrowing needs will be sudden and unpredictable, and will not be related to any long-term capital improvement. The producer security program is not a revenue producing enterprise in the usual sense, although fund assessments could be used to repay WHEDA loans (if authorized by the Legislature). Arguably, the agricultural producer security program serves an important statewide purpose, even if loan proceeds are used to pay individual producers affected by local defaults.

It is not likely that WHEDA would be able to issue a guaranteed "line of credit," so DATCP would have to make a separate loan application for each default (after the default occurred and producer claims were determined). The application and approval process would take time, so there would be no immediate payment to producers. If WHEDA granted the application, it would need to sell bonds to finance the loan. WHEDA might not be able to finance large backup loans required for major defaults. Interest rates might compare favorably with other sources (because WHEDA bonds are tax-exempt), but it is not clear whether there would be significant interest savings.

If DATCP were to seek loans in anticipation of *possible* defaults (which had not yet occurred), the agricultural producer security fund might be saddled with interest costs for loans not actually needed. These costs could easily exceed the cost to acquire a guaranteed "line of credit" from a surety company (as proposed in the department's legislation).

5. Backup Loans From the Board of Commissioners of Public Lands

- **Description.** Under this alternative, DATCP would seek loans from the Board of Commissioners of Public Lands ("the Board") to pay producer default claims that exceed the capacity of the fund. The Board would make the loans, pursuant to ch. 24, Stats., from trust funds created under ch. X of the state constitution. DATCP would repay the loan principal and interest from the agricultural producer security fund.
- **Problem.** The Board administers the following trust funds, which are created by the state constitution and funded from public land sales and other sources: (1) the common school fund; (2) the normal school fund, (3) the university fund and (4) the agricultural college fund. Under the constitution and statutes, trust fund moneys can only be invested in certain ways, and can only be loaned to certain public entities (mainly schools and municipalities) for certain purposes related to the constitutional purposes of the funds (see ch. 24, Stats.).

Current law does not authorize the Board to invest trust funds in, or lend trust funds to, the agricultural producer security program. There is also some question whether the Legislature could, consistent with constitutional intent, change the law to create such authorization. Even if the statutory and constitutional issues could be resolved, a number of serious obstacles would remain.

The Board of Commissioners of Public Lands issues individual loans based on the Board's review of individual loan applications. The Board does not issue "lines of credit" that guarantee, in advance, the immediate availability of loan funds. DATCP would have to submit a separate loan application for each default (after the default occurred and producer claims were determined). Based on DATCP's loan application, the Board would decide whether to approve the loan and whether to loan the full amount requested.

There is no guarantee that the Board would provide the requested loan, in the requested amount. The Board determines the maximum loan amount based on the loan applicant's "tax levy potential" at the time the loan application is made (the Board currently loans only to entities that have taxing authority).

The law currently specifies a maximum loan amount of \$5 million (the approved amount could be less). This may not be adequate to cover a major default under the producer security program. By comparison, DATCP's legislative proposal would provide a "line of credit" for up to \$17 million.

The Board charges interest rates on approved loans, based on private market rates. It is not clear that its interest rate would be any cheaper than the rate charged by a private surety company under DATCP's legislative proposal. The Board normally requires 45-60 days to process a loan application. This would delay any payment to producers, even if the Board ultimately approved the loan request.

6. Backup Loans from the State Investment Board

- **Description.** Under this alternative, DATCP would seek a loan or line of credit from the State Investment Board to pay producer default claims that exceed the capacity of the fund. The Investment Board would make the loans from trust funds or other funds controlled by the Board under ch. 25, Stats. DATCP would repay the loan principal and interest from the agricultural producer security fund.
- **Problem.** Chapter 25, Stats., limits the purposes for which the Investment Board may loan or invest funds. The Investment Board must manage and invest trust funds for the benefit of the trust beneficiaries, and not for other purposes. The Investment Board has advised the department that it may not loan funds to the agricultural producer security fund. An Attorney General's Opinion (December 15, 1987) states that the Investment Board is not authorized to issue a "letter of credit" or to "guarantee" the debt of another. Even if the Investment Board were authorized to provide a loan or line of credit to the agricultural producer security program, the effective charge or interest rate would likely be comparable to that charged by a surety company.

Conclusion

The agricultural producer security fund has a current balance of approximately \$3.4 million. In the absence of a major default, the fund balance will grow steadily. Over time, this will reduce the amount of backup security needed. For the next few years, however, it is important to have a substantial amount of backup security.

DATCP has prepared draft legislation that would authorize DATCP to acquire backup security in the form of a "line of credit" from a surety company. In an open competitive bidding process, a qualified surety company has already submitted a proposal to provide a "line of credit" in the necessary amount (\$17 million) at a competitive market price. DATCP would purchase the "line of credit" with money from the agricultural security fund. If it became necessary to draw on the "line of credit," DATCP would repay the loan principal and interest from the fund.

DATCP has investigated various state-financed backup security alternatives. It does not appear that any of the alternatives provides a readily available source of security, or offers a clear cost advantage at this time.

DATCP – February 25, 2003